COMMONWEALTH OF KENTUCKY
OFFICE OF THE ATTORNEY GENERAL

ANDY BESHEAR
ATTORNEY GENERAL

CAPITOL BUILDING, SUITE 118
700 CAPITOL AVENUE
FRANKFORT, KENTUCKY 40601
(502) 696-5300
FAX: (502) 564-2894

OAG 17-003

March 3, 2017

Subject: Whether a proposed local ordinance that imposes a license tax to companies for the privilege of locating oil and gas wells would violate KRS 353.500(2), which states that the state government has responsibility for regulating all aspects of oil and gas exploration, production, development, gather and transmission.

Requested by: Jamie Hatton, Letcher County Attorney

Written by: Taylor Payne, Assistant Attorney General

Syllabus: The proposed ordinance would not violate KRS 353.500(2) because the Fiscal Court is authorized to levy taxes under KRS 67.083(2) and KRS 353.500(2) is subordinate to the basic powers of municipalities.

Statutes construed: KRS 353.500; KRS 67.083

OAGs cited: OAG 79-385; OAG 95-9

Opinion of the Attorney General

Jamie Hatton, Letcher County Attorney, has requested an opinion of this office to address whether an ordinance proposed for enactment by the Letcher County Fiscal Court ("Fiscal Court") "to impose a . . . license tax that would be charged to Oil and Gas companies for the privilege of locating oil and gas wells within the county" would violate Kentucky Revised Statute (KRS) 353.500(2), which states that the state government has responsibility for regulating all aspects of oil and gas exploration, production, development, gather and transmission. We advise that the proposed ordinance would not violate KRS

353.500(2) because the Fiscal Court is authorized to levy taxes under KRS 67.083(2), and KRS 353.500(2) must be read in conjunction with and subordinate to the basic powers of municipalities. We would also advise that the proposed ordinance should adhere to the principals and limitations set forth by this office in OAG 79-385.

KRS 353.500 was enacted in 1960 as part of the Oil and Gas Conservation Act ("Act"), which was an effort by the General Assembly to encourage the conservation of Kentucky's oil and gas resources. *Smith v. Rogers*, 702 S.W.2d 425, 427 (Ky. 1986); *see also* OAG 95-9. KRS 353.500 is a declaration of the public policy guiding the Act. In particular, KRS 353.500(2) states, in part, "that governmental responsibility for regulating all aspects of oil and gas exploration, production, development, gathering, and transmission rests with state government."

In *Blancett v. Montgomery*, 398 S.W.2d 877 (Ky. 1966), our highest state court at the time addressed the validity of a city ordinance prohibiting exploration for oil and gas within city limits in light of the public policy statement expressed in KRS 353.500(2). The Court held that the statement of public policy found in KRS 353.500(2) "must be interpreted in conjunction with and subordinate to the basic powers of municipalities[,]" such as the authority to create zoning ordinances granted by the General Assembly in KRS Chapter 100. *Id.* at 881. The Court further held that KRS 353.500(2) did not preempt municipalities from regulating oil and gas activities within their city limits under their police power." *Id.*

The Court's holding in *Blancett* governs the question raised before this office. Under KRS 67.083(2), the General Assembly has provided fiscal courts of this Commonwealth the basic power "to levy all taxes not in conflict with the Constitution and statutes of this state now or hereafter enacted." According to *Blancett*, KRS 353.500(2) must be interpreted in conjunction with and subordinate to KRS 67.083(2). Therefore, KRS 353.500(2) neither prohibits nor preempts a municipality from levying a tax simply because the tax will be levied against oil and gas companies. Accordingly, the proposed ordinance for enactment by the Fiscal Court to impose a license fee or tax on companies to locate an oil and gas well in the county would not be in violation of KRS 353.500(2).

In your letter to this office, you note that you have reviewed *C.C.C. Coal Co., Inc. v. Pike County*, 536 S.W.2d 467 (Ky. 1976) and *Shanks v. Kentucky Indep. Oil Co.*, 8 S.W.2d 383 (Ky. 1928) in consideration of the proposed tax to be enacted by the Fiscal Court. As you know, both cases address the difference between a license tax, which municipalities may levy pursuant to Section 181 of the Kentucky Constitution, and other excise taxes, which only the General Assembly may impose. In *C.C.C. Coal Co., Inc.*, the Kentucky Supreme Court held that a tax levied upon the receiving and/or processing of coal at a fixed place of business for distribution was unconstitutional pursuant to Section 181 of the Kentucky Constitution. Id. at 468. The Court recognized that Section 181 prohibits the General assembly from delegating to a subordinate unit of government the power to levy an excise tax, other than license taxes. *Id.* (citation omitted). The Court found that a tax levied upon the receiving and/or processing of coal at a fixed place of business was not a tax on an independent trade, occupation or profession, but on "one of a series of events which occur in the business of production." *Id.* at 468. The Court determined such a tax was therefore not a license tax, but a tax on the use made of coal in the business of production. *Id.* The Court held such a tax was a use tax and that a use tax was an excise tax. *Id.* (citations omitted). As a result, the Court found the tax to be unconstitutional. *Id.*

Upon the Court's rendering of its decision in *C.C.C. Coal Co., Inc.*, this office was requested to address the circumstances under which a fiscal court could enact an occupational or license tax on persons or companies engaging in the severance and processing of coal. In OAG 79-385, this office advised that:

> a county ordinance which levies a license or occupational tax on coal producers engaged in the extractive business enterprise of coal production would be constitutional, provided that the license or occupational tax as applied to coal producers . . . is fairly and equitably integrated with a general county occupational or license tax applying to an overall occupational or license tax. Such a general county occupational or license tax must be based upon reasonable classifications, must not be discriminatory, and must not be arbitrary or confiscatory. Such general tax must be uniform as applied to each classification.

> The trouble with the ordinance in the [*C.C.C. Coal Co., Inc.*] case . . . was that the tax was not levied upon "coal producers" as a license tax. The Pike County coal tax was levied upon the receiving and/or processing of coal at a fixed place of business for distribution. . . . Thus, the [*C.C.C. Coal Co., Inc.*] case suggests, as we just outlined, that the County Phoenix can rise from the ashes of its abortive enactment if the principles and limitations we mentioned are carefully followed. The Pike County coal tax, since it fell short as a license or occupational tax . . ., was merely a tax on certain uses made of coal, and thus was an excise tax.

(internal citations omitted).

Based on your review of *C.C.C. Coal Co., Inc.* and *Shanks*, we would further advise that the ordinance proposed by the Fiscal Court to impose a license tax upon oil and gas companies for the privilege of locating oil and gas wells within Letcher County should adhere to the principals and limitations expressed by this office in OAG 79-385, a full copy of which is attached hereto.

ANDY BESHEAR
ATTORNEY GENERAL

Taylor Payne
Assistant Attorney General

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